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April 24, 2006

Dear Xxxxx:

This letter is in response to your letter dated October 25, 2005 which was addressed to "Retailers Occupation Tax" and your letter dated March 22, 2006, which was addressed to this office, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.tax.illinois.gov to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

We are requesting your guidance in determining whether to charge sales tax to our customers when we invoice them for an optional maintenance agreement. ABC sells and services telecommunications computer equipment primarily to call answering services and centers. We are revamping our maintenance plan offering to include an optional maintenance agreement which price is determined by the type of system and the number of components and positions to be covered. The optional maintenance agreement covers both hardware and software. We do not break out any pricing for the software vs. the hardware and in fact, software is not taken into consideration in our pricing of the maintenance agreement. These agreements are billed monthly or quarterly and can be cancelled with a 30-day notice. Our maintenance contract fees include software upgrades and updates, advance replacement service, telephone support, parts repair and discounts on labor, depending on whether the customer purchases our Economy, Basic or Full Protection Plan.

If you require additional information, I can be reached at #.

DEPARTMENT'S RESPONSE:

In general, maintenance agreements that cover computer software and hardware are treated the same as maintenance agreements for other types of tangible personal property. Please refer to 86 Ill. Adm. Code Sec. 130.1935(b). The taxability of maintenance agreements depends upon if charges for the agreements are included in the selling price of the tangible personal property. If the charges for the agreements are included in the selling price of the tangible personal property, those charges are part of the gross receipts of the retail transaction and are subject to tax. No tax is incurred on the maintenance services or parts when the repair or servicing is performed.

If maintenance agreements are sold separately from tangible personal property, sales of the agreements are not taxable transactions. However, when maintenance services or parts are provided under the maintenance agreements, the service or repair companies will be acting as service providers under provisions of the Service Occupation Tax Act that provide that when service providers enter into agreements to provide maintenance services for particular pieces of equipment for stated periods of time at predetermined fees, the service providers incur Use Tax based on their cost price of tangible personal property transferred to customers incident to the completion of the maintenance service. See 86 Ill. Adm. Code Sec. 140.301(b)(3).

Generally, sales of “canned” computer software are taxable retail sales in Illinois. Sales of canned software are taxable regardless of the means of delivery. For instance, the transfer or sale of canned computer software downloaded electronically would be taxable. However, if the computer software consists of custom computer programs, then the sales of such software may not be taxable retail sales. See 86 Ill. Adm. Code 130.1935(c). Custom computer programs or software must be prepared to the special order of the customer.

Charges for updates of canned software are fully taxable pursuant to Section 130.1935. If the updates qualify as custom software under Section 130.1935(c), they may not be taxable. But, if maintenance agreements provide for updates of canned software, and the charges for those updates are not separately stated and taxed, then the whole agreements would be taxable as sales of canned software.

In addition, you may find helpful information by reviewing the Department’s “Sunshine Letter Rulings” and the above regulations which may be found on the Department’s Internet website under the heading of “Laws/Regs/Rulings.” For example, please see general information letter ST-03-0140-GIL.

I hope this information is helpful. If you require additional information, please visit our website at www.tax.illinois.gov or contact the Department’s Taxpayer Information Division at (217) 782-3336. If you are not under audit and you wish to obtain a binding PLR regarding your factual situation, please submit a request conforming to the requirements of 2 Ill. Adm. Code 1200.110 (b).

Very truly yours,

Edwin E. Boggess
Associate Counsel

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